Creditable Compensation

Police and Firemen's Retirement System

Employees and employers both contribute to the Police and Firemen's Retirement System (PFRS) throughout all employees' careers. These contributions, and the return on their investment, are intended to and normally do provide sufficient funds by the time of retirement to pay lifetime retirement benefits to employees and surviving spouses. Over the past several years, however, some employers and unions have negotiated contracts that restructured employees' pay to substantially increase pensionable salary close to the time they are eligible to retire. When this happens, only a minimal amount of pension contributions are remitted on the improperly increased salaries and insufficient time is available for investment of these contributions before retirement. As a result, the reserves required to pay the increased lifetime retirement benefit are not sufficient and all participating employers are required to make additional employer contributions to compensate for the shortage.

In 2000, the PFRS Board of Trustees approved a revision to the Administrative Code, N.J.A.C. 17:4-4.1, to clarify the definition of creditable compensation, i.e., compensation subject to pension deductions and used to calculate retirement benefits. N.J.A.C. 17:4-4.1 states that "…the compensation of a member subject to pension contributions and creditable for retirement and death benefits in the system shall be limited to base salary, and shall not include extra compensation." Some of the items identified as extra compensation are as follows:

- Overtime
- Pay for extra work, duty or service beyond the normal work day or normal duty assignments
- Bonuses
- Lump-sum payments for longevity, holiday pay, vacation, compensatory time, sick leave, etc.
- Any compensation which the employee or employer has the **option** of including in base salary
- Sell-backs, trade-ins, waivers or voluntary returns of accumulated sick leave, holiday pay, vacation, overtime, compensatory time, or any other payment or benefit in return for an increase in base salary
- Any form of compensation that is not included in the base salary of **all** employees in the same position or covered by the same collective bargaining agreement
- Retroactive increments or adjustments made at or near the end of a member's service, unless the adjustment was made for all similarly situated personnel as a result of an across-the-board adjustment
- Any form of compensation that is not included in a member's base salary during some of the member's service and is included in the member's base salary upon attainment of a specified number of years of service
- Clothing allowances

Stated in a positive manner, creditable compensation consists of pay that meets all of the following criteria:

- Pay for performance of duties required of a PFRS covered position;
- Pay received in a regular paycheck, not in a lump-sum payment;
- Pay not specifically listed as extra compensation or as not being creditable;
- Pay received in a similar manner by everyone else in a similar situation; and
- Pay that is included in base salary from the first day it is paid.

The creditable compensation rule does not prohibit the inclusion of longevity, holiday pay, or education pay in creditable salary. These items can be included if the payments are made as a part of each paycheck for all employees in the same collective bargaining agreement from the time they first receive the compensation.

EXAMPLES

Some examples that should clarify the subject follow.

Example #1 - Situation: the union contract covering a group of employees stipulates that longevity will be included in base salary subject to pension deductions in the 23rd year of service. Prior to that it will be paid outside of base salary.

Determination: longevity will not be considered creditable compensation because it is not pensionable when it is first received and is included in the member's base salary upon attainment of a specified number of years of service.

Example #2 - Situation: longevity is paid to employees beginning in their fifth year. At that time, the employee gets to make an irrevocable decision as to whether to have the longevity pay included in base salary subject to pension deductions for his entire career.

Determination: the longevity is not creditable compensation because its inclusion in base salary is voluntary.

Example #3 - Situation: longevity is paid to employees beginning in their fifth year and is included in base salary subject to pension deductions throughout the employees' careers.

Determination: longevity is creditable compensation because it is paid to all employees in a similar situation and is included in base salary from the first time it is paid.

Example #4 - Situation: a member in his final year of service is due $100,000 for unused vacation and sick pay. The member agrees with the employer to accept $50,000 included in base pay subject to pension deductions as payment for this time.

Determination: the $50,000 is not creditable compensation as it is a trade-in or sell-back.

Example #5 - Situation: A member is covered under a bargaining agreement that does not include longevity as creditable compensation. The member is promoted and now falls under a different bargaining agreement. This agreement does include longevity as creditable compensation for all employees under that agreement.

Determination: Longevity for the newly promoted member is now considered creditable compensation because it is creditable for everyone who is similarly situated, i.e., covered under the same bargaining agreement.

BOARD REVIEW

The Board of Trustees may question the compensation of any member or retiree to determine if all of the reported salary is creditable whenever there is evidence that there may be extra compensation included in the base salary. If the Board determines that there is extra compensation included in the base salary, all employees and retirees affected by that contract will have their contributions on that extra compensation refunded without interest. Retirees will have their retirement benefit recalculated. Contributions remitted by the employer will not be refunded and will be retained in the retirement fund.

A statement as to the creditability of salary in a negotiated union agreement is not binding on the PFRS Board of Trustees and has no effect on the Board’s decision on the inclusion of that salary as pensionable compensation. State statute, N.J.S.A. 34:13A-8.1, states that negotiations cannot annul or modify any pension statute or statutes. The New Jersey Supreme Court has upheld this law and stated that public pensions are sacrosanct, i.e., they are not subject to collective bargaining agreement. The Board of Trustees is the authority on whether compensation is creditable or not for pension purposes.

To assist the PFRS Board of Trustees in fulfilling its obligations to the retirement system and its membership, and assist employer compliancd with the pension statutes, the Division of Pensions and Benefits will periodically request employers to provide a copy of negotiated contracts. The Division will review those contracts to help ensure that compensation practices do not violate creditable compensation guidelines.

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